

Message Text

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C O N F I D E N T I A L STATE 297900 TOSEC 320038

LIMDIS

FOL REPEAT LONDON 19694 ACTION SECSTATE DTD 8 DEC.

QUOTE

C O N F I D E N T I A L LONDON 19694

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E.O. 11652: GDS

TAGS: EFIN, UK

SUBJECT: SITUATION REPORT, DECEMBER 7

REF: (A) STATE 267168; (B) LONDON 19622

1. IMF LOAN CONDITIONS: FINANCIAL TIMES AND TIMES
REPORT THAT THE CABINET IS UNDECIDED ON HOW THE SPENDING
CUTS SHOULD FALL AND THAT NO DECISIONS WERE REACHED AT
MONDAY AFTERNOON'S CABINET SESSION WHICH WAS ATTENDED BY
MR. JOEL BARNETT, MP, CHIEF SECRETARY IN THE TREASURY
WHO IS IN CHARGE OF PUBLIC SPENDING. THE FT ARTICLE
POINTS OUT THAT WHILE THE CABINET'S GENERAL AGREEMENT AT
THE END OF LAST WEEK ON A 2 BILLION POUND REDUCTION IN
PSBR IN 1977-78 WAS BEING PRESENTED BY SOME MODERATE
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OPPONENTS OF DEFLATION AS A COMPROMISE, THE BROAD

ORDERS OF MAGNITUDE DO NOT DIFFER SIGNIFICANTLY FROM THOSE INDICATED TWO WEEKS AGO BY THE CHANCELLOR. DETAILS OF THE PACKAGE ARE REPORTEDLY FAR FROM SETTLED, WITH OPPOSITION FROM ANTHONY WEDGWOOD BENN, ENERGY SECRETARY TO THE PROPOSED SALE OF PART OF THE GOVERNMENT'S HOLDINGS IN BRITISH PETROLEUM.

2. IN THE COMMONS, ROBERT SHELDON, MP, HINTED THAT VAT WOULD NOT BE INCREASED IN THE IMMEDIATE FUTURE, NOTING THE IMPACT ON THE COST OF LIVING AND RETAIL PRICE INDEX OF AN INCREASE IN VAT. HE UNDERLINED THE GOVERNMENT'S INTENTION TO MAKE THE NECESSARY ECONOMIC ADJUSTMENTS OVER STAGES. "THE REDUCTION IN PSBR WILL HAVE TO BE ACHIEVED OVER A PERIOD BY A COMBINATION OF PUBLIC EXPENDITURE AND TAXATION CHARGES. THE STRUCTURAL CHANGES WILL NOT BE THE RESULT OF ONE BUDGET OR ONE PACKAGE BUT A SERIES OF CHANGES AT DIFFERENT TIMES."

3. THE TRIBUNE GROUP OF LEFT-WING MPS WARNED THE GOVERNMENT THAT IT COULD NOT RELY ON THEIR SUPPORT IF ANY FURTHER CUTS IN PUBLIC EXPENDITURE ON SOCIAL PROGRAM AND INDUSTRIAL DEVELOPMENT WERE AGREED TO BY THE CABINET. (THEY ALSO EXPRESSED TOTAL OPPOSITION TO ANY SALE OF PUBLICLY-OWNED ASSETS SUCH AS BRITISH PETROLEUM SHARES.) ABOUT 30 OF THE GROUP'S 70-ODD MEMBERS ATTENDED THE MEETING. ONE LEADING TRIBUNITE HAS TOLD AN EMBASSY OFFICER THAT THE GROUP HAS NOT YET SELECTED A TIME TO WITHHOLD ITS VOTES FROM THE GOVERNMENT AND WILL CHOOSE AN ISSUE WHICH DOES NOT INVOLVE CONFIDENCE. THERE IS ALSO A QUESTION AS TO HOW MANY TRIBUNE MPS ACTUALLY SUPPORT THE PLAN. SHOULD THE TRIBUNITES CARRY IT OUT AND THE GOVERNMENT BE DEFEATED, THE GOVERNMENT WOULD PROBABLY RESPOND AS IT HAS IN THE PAST BY INTRODUCING ITS OWN CONFIDENCE MOTION WHICH WOULD PROBABLY CARRY BY A COMFORTABLE MARGIN. THE TRIBUNE GROUP'S ACTION, ACCORDINGLY, DOES NOT REPRESENT A SERIOUS THREAT TO THE CALLAGHAN GOVERNMENT. AS THE LEFT-WING SEES IT, LIMITED PUBLIC SPENDING CUTS FROM A LABOR GOVERNMENT, WHILE NOXIOUS, ARE STILL INFINITELY PREFERABLE TO THE DEEP CUTS THAT IT WOULD EXPECT FROM A CONSERVATIVE

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GOVERNMENT HEADED BY MRS. THATCHER.

4. ECONOMIC INDICATORS: WHOLESAL PRICES. THE SLIGHT FIRMING OF STERLING IN NOVEMBER CUT THE RATE OF INCREASE IN WHOLESAL PRICES PAID BY INDUSTRY FOR RAW MATERIALS AND FUELS TO 1.25 PERCENT FROM THE OCTOBER INCREASE OF 4.5 PERCENT. YET THIS INDEX IS NOW 29.3 PERCENT ABOVE ITS LEVEL OF A YEAR AGO. WHOLESAL PRICES

OF FINISHED GOODS ROSE 1.7 PERCENT IN NOVEMBER AND STAND 17.5 PERCENT HIGHER THAN IN NOVEMBER 1975. BOTH INDICES REFLECT THE SHARP DECLINE IN STERLING THAT HAS OCCURRED THIS YEAR.

INSTALLMENT BUYING. BRITISH CONSUMERS STEPPED UP THE PACE OF INSTALLMENT BUYING DURING THE AUGUST-OCTOBER PERIOD. IN THE FACE OF STEEPLY RISING INTEREST RATES, THIS BEHAVIOR IS MOST LIKELY DUE TO PRECAUTIONARY PURCHASES IN ANTICIPATION OF RUMORUMORED INCREASES IN THE VALUE ADDED TAX. THE OCTOBER RISE OF 54 MILLION

QIPNM JGWPG CONSUMER DEBT IS THE LARGEST MONTHLY INCREASE IN 1976 AND CAN BE READ AS AN ACCELERATION OF SUCH PRECAUTIONARY BUYING.

RETAIL SALES VOLUME. WITHOUT THE FILLIP OF THE SUMMER TOURIST INFLUX, RETAIL SALES VOLUME DECLINED BY 1.4 PERCENT IN OCTOBER. SALES VOLUME HAS INCREASED BY 2.4 PERCENT OVER THE LAST 12 MONTHS, ALTHOUGH IT IS STILL BELOW MID-1975 LEVELS. ANECDOTAL EVIDENCE POINTS TO HIGHER SALES VOLUME IN NOVEMBER AND DECEMBER FOR THE REASONS OUTLINED ABOVE.

5. YESTERDAY'S AGREEMENT BY THE GOVERNMENT TO THE TUC'S REQUEST TO TAKE ANOTHER LOOK AT A WEALTH TAX (LONDON 19672) IS THE QUID PRO QUO FOR TUC ACQUIESCENCE TO THE GOVERNMENT'S FORTHCOMING AUSTERITY PACKAGE, INCLUDING EXPENDITURE CUTS. THE GOVERNMENT AGREED AT YESTERDAY'S TUC-LABOR PARTY LIAISON COMMITTEE (REFTEL) CONFIDENTIAL

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TO THE SETTING UP OF A JOINT WORKING PARTY, WHICH WILL INCLUDE TWO TUC GENERAL COUNCIL MEMBERS, TWO FROM THE LABOR PARTY NEC, TWO MINISTERS AND TWO LABOR PARTY MP'S. THE COMMITTEE WILL EXPLORE WAYS OF IMPLEMENTING A WEALTH TAX "HOPEFULLY", AS MURRAY SAID YESTERDAY, "WITHIN THE LIFE OF THE PRESENT GOVERNMENT." THERE IS VERY LITTLE LIKELIHOOD THAT THE WEALTH TAX CAN BE PLACED ON THE AGENDA OF THE PARLIAMENT THIS SESSION AND ONE KNOWLEDGEABLE JOURNALIST (PAUL ROUTLEDGE, LABOR EDITOR, "TIMES", DECEMBER 7) SAID: "IT IS DIFFICULT TO SEE YESTERDAY'S COMMITMENT TO A WORKING PARTY AS ANYTHING OTHER THAN A SOP TO UNION OPINION."

WHETHER THE WEALTH TAX HAS A "NEAR FUTURE" OR NOT, IT IS CLEAR FROM OUR TALKS WITH TUC OFFICIALS THAT THE

TRADE UNIONS NEED TO OFFER THEIR MEMBERS SOMETHING NEW TO OFFSET THE BITTER MEDICINE OF THE GOVERNMENT'S AUSTERITY PACKAGE. HOWEVER, IF THE TRADE UNIONS APPEAR READY TO BOW TO OVERWHELMING ECONOMIC NECESSITY, SOME OF THE LABOR PARTY MEMBERS OF THE LIAISON COMMITTEE, ESPECIALLY BARBARA CASTLE AND NORMAN ATKINSON, WERE SHARPLY CRITICAL OF THE GOVERNMENT'S PLAN FOR CUTS.

6. FOREIGN EXCHANGE AND FINANCE. THE GILT MARKET STRENGTHENED AFTER THE ANNOUNCEMENT THAT THE CURRENT LONG-TERM GOVERNMENT TAP STOCK HAD BEEN SOLD OUT. GAINS OF UP TO 5/8 WERE RECORDED AND OVERALL VOLUME WAS THE BEST FOR TWO WEEKS.

THE F.T. INDEX OF 30 INDUSTRIALS ROSE 4.8 TO CLOSE AT 310.1 ON RELATIVELY THIN DEALINGS.

DAY-TO-DAY CREDIT WAS IN SHORT SUPPLY WITH THE BANK OF ENGLAND SUPPLYING LARGE ASSISTANCE TO THE DISCOUNT HOUSES.

STERLING CLOSED AT \$1.6570 MONDAY, A DROP OF \$0.0060, IN SYMPATHY WITH THE WEAKER DOLLAR. THE TRADE-WEIGHTED DEPRECIATION WIDENED TO 45.4 FROM 45.0 PERCENT. THE POUND OPENED TODAY AT \$1.6550.

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ARMSTRONG

UNQUOTE ROBINSON

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